1990 - 91
BUDGET
ADDRESS

NORTHWEST TERRITORIES

91-04598/

PRESENTED BY
THE HONOURABLE MICHAEL A. BALLANTYNE
MINISTER OF FINANCE
AT THE SIXTH SESSION OF THE ELEVENTH LEGISLATIVE ASSEMBLY
FEBRUARY, 1990

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Mr. Speaker, the budget I am presenting today marks the beginning of a new financial challenge for all of us.

In the past ten years, our territorial budget has grown substantially in order to meet the legitimate needs of the population and to introduce the kinds of programs and services available to other Canadians. The growth exceeded the rate of inflation and allowed us to establish programs and services that meet the unique needs of northern residents.

At the same time, we have been able to maintain the lowest tax rates in the country. Our tax structure recognizes the higher cost of living in the Northwest Territories and the need to have tax rates favourable to economic development.

While our expectations have been high, our vision of a northern Territory equipped to take its rightful place within Confederation has been, and remains, reasoned, practical and deliberate. Our vision of the Northwest Territories is clear — a Territory with government institutions that respect cultural values and traditions, that work towards political, social and economic progress and fair treatment regardless of race or sex.

We also know that northern residents, particularly those born and raised here, have a toughness that is seldom found in more urban settings. Boom and bust cycles, although not desirable, are not new to the Northwest Territories. Adapting to changing political, financial and economic environments has been almost a yearly event.

It is in support of this vision, of these realities, Mr. Speaker, that our Government has shaped its budget estimates for the 1990-91 fiscal year.

We may have been dealt a bad hand by the federal government with the imposition of the new Formula Financing Arrangements, but we are not going to let that interfere with the fulfillment of the goals and objectives that we have all been working so hard to achieve. We will have to slow down and shoulder a little more of the expense ourselves, but I am convinced that, with determination, the challenges can be met.

ECONOMIC AND FISCAL CHALLENGES

Mr. Speaker, a major and critical challenge that we will face throughout the 1990's will be to promote economic development. We have a very young population, and these young people will soon be moving into the labour force. We must ensure that there are meaningful job opportunities for our youth.

The Northwest Territories economy was subjected to a detailed review in 1988 and 1989. The Legislative Assembly's Special Committee on the Northern Economy travelled throughout the north to look at the current problems and listen to the concerns and recommendations of the public. As the Committee's report noted, there are a number of structural economic problems. We have a dual economy, one developed, the other underdeveloped. The lack of job-related skills and job opportunities in smaller communities are major impediments to reducing unemployment.

This year, our goal of economic development will be made more difficult to achieve as a result of weakening national and international economies. This weakening may bring down the prices of some of our major exports and slow down the rate of employment growth in the Northwest Territories.

An economic slowdown was already in evidence in the Northwest Territories in 1989. Employment grew at a slower rate than in the previous year and the rate of growth of investment also declined. The economic outlook for 1990 is that there will be little economic growth.

Despite this, there are many bright spots on the economic horizon.

In 1989 the National Energy Board approved an application by Esso Resources Ltd., Shell Canada Limited., and Gulf Canada Ltd. for a license to export 9.2 trillion cubic feet of natural gas to the United States. This is a first step in the development of gas reserves in the Mackenzie Delta/Beaufort region and the creation of jobs for northerners. The progress towards oil and gas development made to date must not be lost. It is critical that the Northern Accord be signed in 1990-91. As Minister of Finance, I will work with the Minister of Energy, Mines and Petroleum Resources and my other Cabinet colleagues to ensure that the Accord will provide appreciable financial and economic benefits to the Northwest Territories from oil and gas development.

In December an agreement-in-principle was reached on the Inuit land claim. It is hoped that both the Inuit and the Dene-Metis claims can be finalized in 1990-91. The settlement of land claims will mean the permanent recognition of the role of northern aboriginal people in shaping social and economic decisions affecting them and in achieving greater economic self-sufficiency. The economic benefits from land claims will be felt by all northerners, not just the immediate beneficiaries.

In the mining industry, we are pleased to see the continued development of the Colomac mine project. At full production, the value of the mine's output would boost gold production in the Northwest Territories by about 50 per cent. We were also pleased by the opening of the new Treminco mill at the Ptarmigan mine eight months ago.

Tourism continues to grow as an important industry, providing opportunities for employment throughout the north. Over the past ten years there has been a tremendous strengthening of this industry and we can look forward to its continued development and to the new opportunities it will provide.

This year, construction will begin on the North Warning System short-range radar sites. Construction of these sites is scheduled for completion in 1993. Of the thirty-six short-range radar installations, thirty-one are to be located within the Northwest Territories. The construction and maintenance of these facilities will benefit northerners.

We are enthusiastic about new and unique opportunities arising from our renewable resource industries. Four years ago, for example, the Baffin offshore shrimp and scallop fishery was virtually non-existent. Now, it provides employment to about 50 persons in the Baffin region. This is an excellent example of what can be achieved when economic development opportunities are identified and seized upon.

Our Government faces some new fiscal challenges in the 1990's.

Last December the federal government announced a new Formula Financing Arrangement, to come into effect on April 1, 1990. I will be addressing the details of the new Formula later in this Address. The immediate financial impact of the new arrangement is a reduction in our 1990-91 grant of about $25 million from what we would have received under the old Formula. Over the next five years the reductions will amount to about $110 million. Not only are these cuts damaging to the Government's fiscal position, and to our ability to respond to the pressing needs of our residents, but the new Formula contains serious flaws which will limit our ability to develop the northern economy.

Mr. Speaker - economic development, control and development of our natural resources, both renewable and non-renewable, protection of the environment, settlement of aboriginal claims, Formula Financing - these are the challenges we face. Our response will set the course for the next decade. The fiscal strategy that we adopt now can either tie the hands of future governments or give them the flexibility they will need to reach their goals.

FISCAL STRATEGY

Changes to Formula Financing mean that our revenues will grow by less than inflation in 1990-91. Our spending cannot continue to grow the way it has in the past.

We must make some tough choices. We can still manage under the new Formula, if we are careful. We must all be prepared to reduce our expectations and to bear part of the burden. Unless we limit our expenditure growth, it will not be long before we have to borrow. Debt charges would then have to be paid with dollars taken from badly-needed programs. If we do not act responsibly over the next few years we could find ourselves, like the federal government, burdened with debt and paying over 30 cents of every tax dollar to finance the debt.

In the long run, that leaves us with only one responsible approach - a balanced approach using both reduced expenditure growth and modest increases in taxes. Although, under the new Formula, the federal government is forcing us to increase taxes, we simply do not have the fiscal capacity to replace the entire amount of the federal cuts this way. Therefore, we must rein in our expenditure growth. We must realize that we cannot immediately do everything we want to. We must establish our expenditure priorities.

The decisions the Government has made, Mr. Speaker, reflect this balanced approach to our fiscal realities:

- Expenditures, after adjustment for inflation, will be less than last year;
- Tax increases have been kept to a minimum;
- We will incur a small manageable budgetary deficit to cushion the impact of the federal cuts.

Mr. Speaker, this represents a reasoned, balanced use of our accumulated surplus over the next two "transitional" years. In the long run, we will continue to strive for a balanced budget.

These measures are necessary to preserve the fiscal integrity of the Government of the Northwest Territories and to ensure that we have the flexibility to meet current and future challenges.

They will affect everyone - all departments, all government boards and agencies, all municipalities. The Government of Canada is attempting to reduce its unmanageable budgetary deficit. Federal transfers to the provinces have been subject to restraint for a number of years. We could not expect to remain unscathed. We must all be prepared to do our part. We must all recognize that the old days are gone. We

cannot ignore the circumstances that we have been forced into. We must face the problem now, not later.

Mr. Speaker, later in this Session, the Government will be tabling its economic development strategy. The fiscal strategy we are adopting in this budget is an essential element of that strategy. Without a sound fiscal policy, there cannot be a successful economic strategy. A government so burdened with debt that it lacks the resources to provide essential services is powerless to promote economic development. A government which must continually increase taxes to finance ever-increasing expenditures will eventually stifle incentive and drive investment elsewhere.

Over the long run, a sound fiscal policy means living within our means.

BUDGETARY EXPENDITURES

Total expenditures this year are projected to be $1 billion. Voted expenditures will increase by $5 million over 1989-90 revised estimates. After estimated supplementary requirements and lapses are accounted for, expenditures in 1990-91 will increase by $26 million, or 2.7 per cent over those of 1989-90. This is considerably lower than our average rate of spending growth of 10 per cent over the five years of the old Formula. Given expected inflation of 4 to 5 per cent, this $26 million represents a cut in real expenditures.

The Government established the initial 1990-91 budget after carefully considering expenditure needs that were submitted by all departments. Following the announcement of the changes to Formula Financing it was necessary to re-examine this plan and make serious expenditure cuts and reallocations in order to increase expenditures in priority areas.

As a result, all government departments and all government funded bodies must tighten their belts. We must all take stock and plan for a new era.

- The growth of the civil service has been halted. In fact, in 1990-91 there will be a small cut in the size of the civil service.

- Growth in contributions to government funded bodies will be constrained. However, no operating contributions to organizations primarily funded by Government will be reduced below the level of support provided in 1989-90.

- Capital spending has been kept at $161 million, virtually unchanged from 1989-90 levels.

ECONOMIC DEVELOPMENT INITIATIVES

As I mentioned earlier, economic development remains a priority of this Government. I would like to present some of the budgetary initiatives being undertaken in 1990-91 in support of the development of our economy.

Expenditures by the Department of Economic Development and Tourism will total $38.8 million in 1990-91. The Northwest Territories Development Corporation, scheduled to be established at the beginning of the fiscal year, will allow the Government to actively participate in business development, either as the sole investor, or by providing equity capital in joint ventures with the private sector. The Government has allocated an initial $2 million in investment capital to the Corporation in 1990-91. The Corporation forms one part of the Department's economic development strategy, aimed at employment creation and stimulation of the economy.

The Department has been allocated a $9.2 million capital budget in 1990-91, an increase of $5.8 million over the current year. This reflects increased activity in the development of facilities designed to increase tourism. The Baffin Cultural Centre will be constructed at a cost of almost $3 million. This is a joint project with the Department of Culture and Communications, which will be funded out of the Department of Economic Development and Tourism's capital budget. The Centre will promote tourism throughout the Baffin Region. It will provide a focal point for information about tourist attractions and facilities and about locally produced arts and crafts.

Together, the Departments of Culture and Communications and of Economic Development and Tourism will provide over $400,000 in capital funding to restore and develop historic sites. Culture and Communications will also spend over $1 million for the construction of the Cape Dorset Community Museum.

Economic Development and Tourism will promote the development of the fishing industry in the Baffin Region through the purchase of a $350,000 demonstration vessel to test various fishing methods and technologies. The arts and crafts industry will benefit from more than $400,000 in capital contributions.

Education is of critical importance in maximizing the positive effects of many of the other strategy-driven initiatives being undertaken. The greatest potential for reducing unemployment will be achieved by educating and training Northwest Territories residents to fill existing and future jobs. The Department of Education initiatives, therefore, fill a key role in the strategy. The Department's efforts involve the schools, Arctic College, literacy programs, and federally and territorially supported employment initiatives.

Spending by the Department of Education will increase by $10.7 million in 1990-91

to $181.6 million. Almost $2 million in new funding will be allocated to programs designed to provide training and jobs to northerners. Of this, over $580,000 will go to help private sector employers hire and train northerners as apprentices. The Training on the Job Program will be expanded. This program provides salary subsidies to the private sector to hire and train northern residents. An additional $500,000 has been allocated to this program. A total of $800,000 will be used to fund Northwest Territories native organizations to train native leaders for the administration of Land Claims settlements and to increase the number of native teachers in the Northwest Territories school system.

Funding for the Student Financial Assistance Program has been enhanced by over $600,000 to provide scholarships and enhanced accommodation and transportation benefits, and to increase existing benefits in recognition of the higher living costs faced by post-secondary students.

The Department will begin construction of new schools in Paulatuk, Broughton Island, Baker Lake, Colville Lake and Rae. A new adult education centre will be built in Arviat and existing centres in Hall Beach and Repulse Bay will be upgraded.

Transportation remains an essential element in the development of the Northwest Territories economy.

The Government has allocated $37 million to the Department of Transportation in 1990-91. The Department is actively pursuing the transfer from the federal government of responsibilities for transporation. Negotiations for the transfer of responsibility for the Inter-Territorial Road Program and Arctic B & C airports are virtually complete. The highway transfer agreement is expected to be signed within the next few months, taking effect retroactively to April 1, 1989. The airports transfer should be finalized over the winter and come into effect on April 1, 1990.

The Department is also concentrating efforts on the improvement of the most heavily-travelled road in the territories, the road from the Alberta border to Yellowknife. Over the next decade, it is hoped to have most of this highway upgraded.

This past year, the Government of the Northwest Territories and the federal government began work on a special joint study to develop a Northwest Territories Transportation Strategy. This strategy, when complete, is meant to encourage and support transportation developments over the next 20 years.

SOCIAL PROGRAMS

Despite the necessity for overall government financial caution, this Government remains committed to providing the social programs which form an essential component of family and community well-being in the north.

Alcohol and drug abuse continues to contribute to the breakdown of community and family life. The Department of Social Services will spend almost $6.0 million over the next two years to construct and provide operating funding to two treatment centres for alcohol and drug rehabilitation.

The construction of the Somba K'e Treatment Centre, between Yellowknife and Dettah, and the Alcohol Treatment Centre on the Hay River Reserve will almost triple the number of bed-spaces currently available in the Northwest Territories for alcohol treatment. The Department's long-term strategy also includes the construction of a treatment centre in the eastern Arctic. The operating costs of the new treatment centres will be offset by an increase in alcohol prices. An additional $400,000 has been allocated to meet the increased demand for funding for community and band alcohol and drug prevention projects.

The Department will also allocate additional funds to meet the demand for child sexual abuse treatment and prevention services. These resources will be used to respond to the increased number of reported cases of child sexual abuse throughout the Northwest Territories.

The provision of quality health services in much of the north depends on the presence of highly skilled community health nurses. The Department of Health will spend an additional $400,000 in 1990-91 to provide advanced skills training for community nurses.

The effects of environmental contaminants in food, especially in country foods, continue to worry northerners. The Department will be establishing an environmental contaminants unit responsible for providing the general public and interested groups with information on contaminants and their potential impact on human and animal health. The Department of Renewable Resources has also allocated funding of almost $200,000 to monitor contaminants and diseases in wildlife and country foods.

The Government remains committed to improving the housing conditions of territorial residents. This budget will provide the Northwest Territories Housing Corporation with funds to construct another 300 new units of social housing across the Northwest Territories and replace 100 aging Northern Rental houses.

The Housing Corporation will be implementing new program initiatives during the coming fiscal year to broaden eligibility for home ownership by a wider spectrum of territorial residents. A total of $625,000 has been allocated to the Rental Rebate Program and the Access Program. In time, these initiatives will enable greater numbers of families to house themselves and reduce dependence on government assistance.

Mr. Speaker, I would now like to address two issues which Cabinet took into consideration when making decisions about taxes.

FORMULA FINANCING

The federal government has significantly altered the Formula Financing Arrangement under which our annual grant is determined. The new arrangements take effect in 1990-91 and will be in place for five years, subject to a review after three years.

As a result of the federal changes, our funding will be tied to an indicator based on provincial and territorial tax effort in 1987-88. The result is a reduction in our grant because the federal government considers the tax effort of our Government to be lower than the provincial average for that year. In addition, federal grants in subsequent years will be reduced according to how we have lagged behind the growth in provincial tax effort since 1987-88.

Mr. Speaker, this change has fundamental consequences for our expenditure and taxation policies over the next five years.

We would have to impose the same taxes as the provinces, at rates comparable to the provincial average in order to recover the cuts imposed by the federal government. We would also have to keep up with increases in provincial tax effort to protect our total funding from further erosion.

This provision of the Formula ignores the fact that northern residents already face a higher tax burden than other Canadians when the high cost of living in the north is taken into account. It also ignores the fact that we must be careful not to introduce drastic tax changes which would seriously harm incentives to work and do business in the Northwest Territories.

In fact, the Formula as a whole acts as a disincentive to economic development. However, this disincentive will not detract us from our goal of developing the economy of the Northwest Territories.

There are some positive elements of the new Formula. The most important of these is that the Formula now takes population into consideration. We have argued for this change for several years. As a result, some of the reductions resulting from the tax effort change will be partially offset by the population adjustment. This is because the population of the Northwest Territories is expected to grow at a faster rate than that of the rest of Canada over the next five years.

One other positive element of the new Formula is our expectation that a five-year arrangement will allow us to plan our fiscal strategy without the threat of further direct federal cuts to our grant.

In addition, representations by the Government and by the Chairman of our Standing Committee on Finance, supported by the hard work of the officials of my Department, have resulted in a Formula that includes other elements designed to further reduce the impact of the tax effort adjustment factor. Firstly, the reduction is not as large as was originally proposed by the federal government. Secondly, there will be a phase-in of the financial impact over three years.

Despite these hard-won concessions, the Government of the Northwest Territories remains fundamentally opposed to the application of the tax effort adjustment to the Formula. Its use produces a Formula which is flawed and its imposition by Canada will have severe financial consequences for our government over the next five years.

GOODS AND SERVICES TAX

Another federal government initiative, the Goods and Services Tax, or GST, is also a source of serious concern.

The federal government will introduce the GST in 1991. I have argued against the tax in its proposed form because it is inequitable, and will reduce our relative competitiveness with southern Canada.

Let me give you our main objections:

- First, the tax will result in residents of the Northwest Territories paying more sales tax than other Canadians for the same goods and services. The current federal sales tax, to be replaced by the GST, is levied at the manufacturers' level. Because the GST is applied at the retail level, the large component of transportation costs and higher northern margins that is not currently fully taxed, will be fully taxed under the GST.

- Second, higher incomes in the north will result in residents with the same 'real' purchasing power as southern Canadians benefiting less from the enhanced federal sales tax credit.

- Third, the GST has the potential to seriously reduce our competitiveness compared with southern Canada. The tax will make the Northwest Territories an even higher cost region in which to do business and, therefore, a less attractive

place in which to invest. This will certainly retard our economic development.

- Finally, the residents of the Northwest Territories already face a high tax burden. The GST will further limit the tax room available to the Government of the Northwest Territories. This is particularly ironic since the federal government is penalizing this Government for having what they perceive to be a low tax effort.

I advised the Honourable Michael Wilson of our objections on a number of occasions. I also tabled a brief with the House of Commons Standing Committee on Finance and persuaded the Committee's Chairman, Mr. Blenkarn, to send members of his Committee to the Northwest Territories to hear first hand what northerners had to say. I will continue in my efforts to have our views heard and the inequitable treatment of northerners addressed.

REVENUE INITIATIVES

Mr. Speaker, as I have mentioned, the grant from Canada will be approximately $25 million lower than under the previous Formula. This is a permanent, rather than a one-time reduction. Presently 85 per cent of our funding comes from the federal government. Only 15 per cent is raised through our own revenues. Under the new Formula, we will be forced to bear more of the burden of our own expenditures.

I am announcing, this afternoon, changes to tax and other revenues which will generate a total of $5.3 million in additional revenues in the coming year. However, this budget does not introduce a Northwest Territories sales tax.

In 1988 I initiated extensive consultations on Northwest Territories tax policies. I released a major document entitled "Northwest Territories Tax Options" and distributed over 20 thousand pamphlets, in all communities, that summarized our tax options. On a number of occasions I met with representatives from different community groups. Following these consultations, the Government considered a number of options. Decisions were influenced by the views we received from taxpayers and respected the criterion that any tax changes, taken as a package, should not hold back the economic development of the north.

It is regrettable that the federal cuts have come at a time when our small business sector is struggling to establish itself in most of the Northwest Territories. Any tax increases have the potential to hurt the economy of the Northwest Territories, but it is our small business sector which is most vulnerable.

We have decided to address this. I am pleased to announce that a new, lower corporate income tax rate of 8 per cent will apply to the first $200,000 of taxable active business income of private Canadian-controlled corporations. This measure is effective January 1, 1990. It is estimated that 90 per cent of companies which are based here and pay taxes here can benefit from this reduction.

This rate is lower than the equivalent rate in all provinces except Quebec and Yukon.

Income in excess of $200,000, and income earned by public and non-Canadian controlled corporations will be taxed at a higher rate of 12 per cent instead of the current rate of 10 per cent. This rate is also lower than all the other provincial rates except those of Quebec and Yukon.

A modest increase to the personal income tax rate as well as to the corporate income tax rate is an equitable way to spread the burden of our revenue needs among all Northwest Territories taxpayers according to their means. I am announcing an increase of one percentage point in the Northwest Territories income tax rate for individuals. The rate will be increased from 43 to 44 per cent of Basic Federal Tax. This rate is still the lowest of any province or territory in Canada. It will be effective for all income earned in 1990.

For a taxpayer with no dependant and an income of $45,000, this represents an increase in Northwest Territories income tax of $72 per year. The reduction in the federal grant in the upcoming year represents approximately $475 per person in the Northwest Territories. The increase in the income tax rate will offset only a small portion of that reduction.

Health care costs are a large and growing part of the expenditures of the Government. Considerable resources are also spent educating residents on the health risks of smoking and drinking. I am introducing several measures today, which in addition to increasing revenues, will provide an additional incentive for people to follow a more healthy lifestyle.

Effective April 1, 1990, liquor commission mark-ups on alcohol will be increased to generate an additional $1.8 million annually from the sale of liquor and beer. The impact of the increase will be an 8 per cent price increase for wine and spirits, and a 5 per cent increase in the price charged for beer. The revenues generated from these increases will offset the costs of the new alcohol and drug treatment measures I announced earlier.

Also on April 1, 1990, the tax rate on cigarettes and most other forms of tobacco will go up from 55 per cent to 60 per cent of the price. This change will increase the cost of a carton of cigarettes by about one dollar, with corresponding increases to the prices of most other tobacco products.

I will be introducing legislation for these tax changes during this session of the Legislative Assembly.

CONCLUSION

Mr. Speaker, the funding growth provided for under the previous Formula Financing Arrangement allowed our Government to increase its expenditures and to address a substantial number of legitimate program needs.

However, the new Formula arrangements mean new rules, and lower funding expectations. The expenditure growth we have been able to accommodate in the past cannot be maintained.

This Government has taken a balanced and reasoned approach to our new fiscal realities. Expenditure growth has been cut, tax increases have been kept to a minimum, and during this coming transition year, we will incur a manageable budgetary deficit.

The Government of the Northwest Territories is in good fiscal shape. We are in better shape than other Canadian jurisdictions. We still have among the lowest tax rates in Canada and we are free of the burden of a large public debt.

It would be irresponsible to jeopardize this. We have to make some tough decisions about our future. We must reduce our expectations, and be willing to do more with less. I believe, Mr. Speaker, that northerners can meet this challenge.

APPENDIX A

FISCAL POSITION

TABLE A1
GOVERNMENT OF THE NORTHWEST TERRITORIES
PROJECTED FISCAL POSITION AT MARCH 31, 1990
$ (millions)

	1988-89 Final Results				1989-90 Projected Results			
	1989-90 Budget Address	1988-89 Actuals	Increase (Decrease)	Explanation	1989-90 Budget Address	Current Forecast	Increase (Decrease)	Explanation
Revenues	872.9	876.8	3.9	Higher P/L escalator	943.0	955.5	12.5	$4.8 million, federal share of fire suppression over-expenditures; $5.1 million, federal share of health cost increase; $2.6 million, escalator changes.
Expenditures	852.1	858.0	5.9	Higher O&M expenditures than anticipated	954.4	975.5	21.1	$6.5 million, health cost increases; $9.5 million, fire suppression over-run; higher capital carry-overs from 1988-89
Annual Surplus (Deficit)	20.8	18.7	(2.1)		(11.4)	(20.0)	(8.6)	
ACCUMULATED SURPLUS (DEFICIT)								
Opening Balance	41.8	41.8	0.0		61.2	66.9	5.7	Higher capital carry-overs
Allocation to Business Loan Fund and Student Loan Fund	(1.5)	(0.5)	1.0	Anticipated Business Loan Fund increase did not materialize	(2.5)	(5.0)	(2.5)	Increase in Business Loan Fund limit.
Prior Year Adjustment		6.8	6.8	Recoveries of prior years' expenditures				
Annual Surplus (Deficit)	20.8	18.7	(2.1)		(11.4)	(20.0)	(8.6)	
Closing Balance	61.2	66.9	5.5		47.2	41.9	(5.3)	

APPENDIX B

ECONOMIC SITUATION AND OUTLOOK

THE ECONOMY IN BRIEF

The economic base of the Northwest Territories is relatively narrow. The extraction of non-renewable resources for export dominates goods production. Construction is the second largest goods producing industry. Manufacturing, renewable resources and commercial agriculture account for a very small portion of total economic activity, equivalent to less than one per cent of Gross Domestic Product (GDP) in 1988.

The service sector is large. It accounts for over four fifths of Northwest Territories employment, well above the 75 per cent average for the Canadian economy as a whole. As a share of territorial output, the service industries accounted for 57 per cent of GDP in 1988. Government, broadly defined, is the major component of this sector and accounted for 44 per cent of total Northwest Territories employment and 31 per cent of all Northwest Territories investment in 1988. Other important service sector industries are transportation, trade and business and personal services, which includes tourism firms.

The economy of the Northwest Territories continued to grow in 1989, albeit at a slower rate than in 1988. Employment is forecast to have grown 2.8 per cent, much lower than the 1988 growth rate of 7.1 per cent. Investment is projected to have increased by approximately 9.3 per cent in nominal terms, with housing investment projected to have increased by 11.8 per cent.

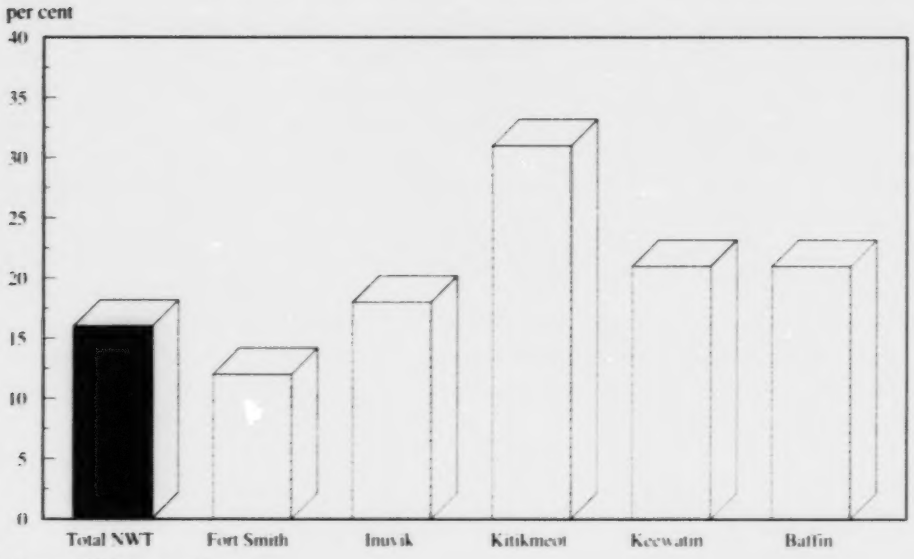
Overall, renewable resource production last year was relatively weaker, with the total value of output falling from $9.8 million in 1987-88 to $8.0 million in 1988-89. The value of fur output in the 1988-89 harvest year decreased by 27 per cent to $4.4 million from $6.1 million in 1987-88. The value of the fish harvest is forecast to have decreased by over 20 per cent in 1988-89. Lumber production is estimated to have risen from $1.0 million to $1.5 million.

The unemployment rate remains high. A survey by the Government of the Northwest Territories Bureau of Statistics has established it at 16 per cent in the first quarter of 1989 with wide variations between regions: Fort Smith, 12 per cent; Inuvik, 18 per cent; Kitikmeot, 31 per cent; Keewatin and Baffin, 21 per cent.

INTERNATIONAL AND NATIONAL ECONOMIC ENVIRONMENT

United States and overseas economies continued to grow in 1989, though economic performance was weaker relative to 1988. Real GDP in the United States is projected to have increased by 2.2 per cent in 1989, half its rate of growth in 1988.

CHART B1
REGIONAL UNEMPLOYMENT RATE, 1989



Source: GNWT Bureau of Statistics

Despite this slowing rate of economic expansion, labour and product markets remained tight in 1989. Given growing inflationary pressures, the United States Federal Reserve and European central banks moved to dampen inflation by increasing interest rates. Late in 1989, the United States Reserve eased its monetary stance when economic growth showed signs of rapid deceleration.

Canada's real economic growth, like growth in most other industrialized countries, is forecast to have declined in 1989. Real GDP growth is forecast to have fallen to about 2.5 per cent from an impressive 5 per cent growth rate in 1988.

Like the United States, Canada faced mounting inflationary pressures last year, with consumer inflation rising to five per cent. The national unemployment rate reached its lowest level since 1981, 7.5 per cent. Consequent pressure in labour markets contributed to relatively higher wage settlements, increasing the likelihood of higher inflation.

Unlike in the United States, inflationary pressures in the Canadian economy do not appear to have abated, reducing the opportunities for interest rates to fall in 1989. The forecast reductions in economic growth — to less than two per cent in 1990 — and slackening in the labour market will likely allow for modest reductions in interest rates this year.

Measures to reduce interest rates in the United States without corresponding initiatives in Canada contributed to a strong Canadian dollar. Late in 1989, the value of the Canadian dollar relative to the United States currency exceeded US$0.86, the highest level since 1980.

A relatively strong performance of the Canadian dollar in 1990 will continue to adversely affect producers of gold and other metals in the Northwest Territories. Since the majority of mineral output is destined for export markets, and because the value of output is set internationally and is denominated in the United States dollar currency, Canadian producers are less competitive as the Canadian dollar appreciates in value. Since prices for major minerals, including oil, are set in United States dollars and producer costs are largely incurred in Canadian dollars, producer margins decline as the Canadian dollar appreciates.

Continued high interest rates will dampen investment in the Northwest Territories. Private sector business investment growth is likely to weaken as debt costs induce capital spending restraint. The high cost of consumer borrowing will cause personal expenditure growth to deteriorate with adverse effects on the residential construction industry.

The continuing slowdown in economic growth into 1990 will contribute to reduced demand for lead and zinc. Demand for these minerals is tied to overall international economic conditions. As economic growth slows, the growth in demand for products incorporating lead and zinc, particularly automobiles, should also decline.

THE NORTHWEST TERRITORIES ECONOMY

POPULATION

The rate of population growth in the Northwest Territories remains substantially above the Canadian average. Between July 1, 1988, and July 1, 1989, total population increased by 1.9 per cent, or 1,000 persons, to 53,300. This high population growth contrasts with the 1986-87 situation when population actually declined, principally because of large net out-migration from Pine Point and Inuvik.

The principal source of population increase was natural population growth. In 1989, the birth rate is projected to have been 2.5 per cent compared to 1.4 per cent for Canada as a whole. Net migration, on the other hand, tends to be negative. Out-migration has exceeded in-migration since 1985. In 1989, net out-migration is likely to be approximately 100 persons, down from 382 persons in 1988 and 1,075 persons in 1987.

Northwest Territories residents are generally younger than Canadians as a whole. Persons 19 years of age or younger, for example, comprised 43 per cent of the population in 1986, compared to 26 per cent for Canada as a whole. This very young population sustains pressure for government to maintain a greater quantity of education and other services targeted for children and youth.

MINING

Mining is a cornerstone of the Northwest Territories non-traditional economy. The six operating mines — four gold and two lead-zinc mines — employed approximately 1,800 persons in 1989, or one of every two workers in the goods producing sector.

Total mineral production is forecast to have fallen sharply in 1989 due to the cessation of milling operations in Pine Point early in 1988. Consequently, the volume of lead and zinc produced in 1989 shows a sharp decline. Lead output is projected to have declined by 58 per cent to approximately 27 thousand tonnes and zinc production to have declined by 39 per cent to approximately 178 thousand tonnes.

The volume of gold production is forecast to have increased marginally to about 11.6 thousand kilograms. The volume of silver production declined about 23 per cent to 17.5 thousand kilograms, primarily because less silver was produced as a by-product of the lead-zinc operation at Nanasivik.

Gold production will increase sharply in 1990 if the Colomac mine is brought on stream as projected. At full capacity, the mine could produce in excess of 5.5 thousand kilograms of gold per year. Such a level of production would increase the Northwest Territories' current annual gold output by approximately fifty per cent.

The reduction in the volume of mineral production last year will be partially offset by the good price performance of some of these commodities. In particular, lead prices were up slightly in 1989 while zinc prices posted large gains. Overall, zinc prices averaged approximately 38 per cent higher in 1989 than in 1988, though they declined sharply late last year. The buoyant zinc market delivered substantial benefits to the Northwest Territories' two zinc producers. Zinc accounts for over half the value of mineral shipments from the Northwest Territories.

In contrast, although the price of gold rebounded late in 1989, gold prices were, on average, about 15 per cent lower last year.

The rise in the value of the Canadian dollar in 1989 cut into mineral producers' margins. A weaker dollar in 1990, as projected by most economic forecasters, will benefit the Northwest Territories mining industry.

Lower mineral exploration activity last year may have resulted from the mixed performance in the mining industry and changes in tax policies, in particular the reduction of incentives provided by flow-through shares. A survey conducted by the Northwest Territories Chamber of Mines suggests total exploration expenditures in the Northwest Territories in 1989 declined by 26 per cent to $83.8 million from $112.6 million in 1988. As in previous years, most exploration activity in 1989 was concentrated in the Mackenzie region.

OIL AND GAS

Oil production in the Northwest Territories increased moderately in 1989. Production at the Norman Wells field, the source of virtually all oil produced in the Northwest Territories, is projected to have risen to 11.2 from 10.9 million barrels in 1988, an increase of approximately three per cent and the sixth consecutive year-over-year increase in the volume of Norman Wells output. The production of natural gas in 1989 is forecast to have fallen 22 per cent to approximately 8.0 from 10.3 billion cubic feet in 1988. Output of gas declined at both Norman Wells and Pointed Mountain, the fourth consecutive year of gas production declines for both fields.

A very positive signal for the oil industry in Canada was the rebound in oil prices. After declining about 20 per cent in 1988, crude oil prices rose to average approximately US$20, about 11 per cent higher in 1989 than 1988. Most forecasters currently anticipate the price of oil to remain in the US$20 per barrel range through 1990.

Oil and gas exploration and development activity rose last year. Ten major drilling programs were undertaken, six onshore and four offshore. Conoco, Chevron, Shell and Paramount undertook mainland drilling, while the offshore drilling projects were undertaken at different locations in the Beaufort Sea.

This compares favourably to the seven drilling programs that were completed in 1988. All four offshore drilling programs in 1988 were at Gulf's Amauligak field.

Seismic exploration activity in the Northwest Territories in 1989 approximated 1988 levels. In 1988, 11,500 kilometres of seismic data was acquired in the Mackenzie Delta/Beaufort, versus 12,200 kilometres in 1989. Seismic programs on the Northwest Territories mainland declined slightly last year, down to 1,600 kilometres from 1,700 kilometres in 1988.

Preliminary indications are that oil and gas drilling activity in the Northwest Territories this year will approximate 1989 levels. Eight more drilling projects are currently planned.

Last year, the National Energy Board approved an application by Esso Resources Ltd., Shell Canada Ltd. and Gulf Canada Ltd. for a license to export 9.2 trillion cubic feet of natural gas to the United States. This is a first step in planning the development of gas reserves in the Mackenzie Delta/Beaufort.

While this project may not carry immediate benefits, only bringing gas to market in 1996 or later, the project would necessitate that construction of the field and pipeline facilities begin in the first half of the 1990's. Clearly, such a project could have an enormous impact on the Northwest Territories economy.

The Government of the Northwest Territories is continuing discussions with the federal government for the transfer of oil and gas management and administration responsibilities, including the ability to collect oil and gas resource revenues.

CONSTRUCTION

Total construction expenditures in 1989 were projected to have risen 21.6 per cent to $700 million, based on Statistics Canada's survey of private and public investment intentions. Private sector construction investment was projected to have increased to $374 million last year, an increase of two per cent over 1988. Public sector investments were projected to have increased 56 per cent to $326 million.

Housing sector investment continued to grow last year at a healthy pace. In 1989, housing sector investment is forecast to have increased by 11.8 per cent after posting a 10.3 per cent increase in 1988.

RENEWABLE RESOURCES

Renewable resource industries — forestry, fishing, hunting and trapping — are extremely important to the many small producers throughout the north. These industries provide cash incomes, facilitate the maintenance of traditional lifestyles and encourage employment and local production in the other economic sectors of the regions.

The value of the fish harvest in the 1988-89 fishing season (May to April) is estimated to have declined to $2.1 million from $2.7 million in 1987-88. The fishery employs about 325 persons, mostly on a seasonal basis. Whitefish production from Great Slave Lake accounts for about 60 per cent of the value of output, with the Arctic char harvest accounting for a further 20 per cent.

Lumber production in the Northwest Territories was approximately six million board feet in 1988-89. The value of lumber produced was approximately $1.5 million.

Almost 90 per cent of commercial lumber production came from the Hay River mill. About 50 people are employed by the lumber industry as loggers and sawmill workers, mostly on a seasonal basis. Several communities in the south Mackenzie region have sawmill operations for local consumption, but climate and geography limit widespread expansion of this industry.

1988-89 was a poor season for fur production. After rising to a record high of $6.1 million in 1987-88, the value of fur production declined sharply in 1988-89 to $4.4 million. Both prices and production were down. The value of marten production, in particular, dropped sharply to $2.6 million, a decline of 35 per cent from 1987-88. Muskrat production also posted a sharp decline, from $196,000 to $32,000 in 1988-89. Overall, the prices of furs and hides in 1989 were about 17 per cent lower than in 1988.

About 3,000 persons earn income from hunting and trapping in the Northwest Territories. There are also two commercial silver fox fur farms.

ARTS AND CRAFTS

Arts and crafts contributes about $22.5 million of production to the Northwest Territories economy. Over half of the value of output originates from the Baffin region, where opportunities for employment in the wage economy are limited. About 3,500 persons are estimated to derive some income from arts and crafts production. The vast majority of producers must supplement their income from arts and crafts because of low producer returns.

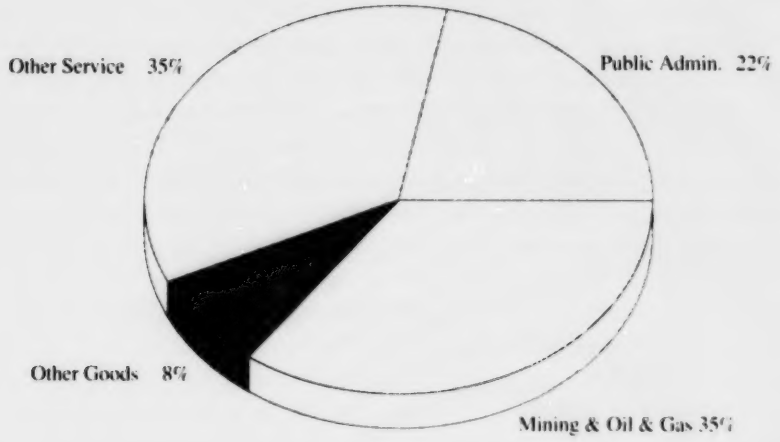
THE SERVICE INDUSTRIES

Altogether, the service sector accounts for 82 per cent of Northwest Territories employment and about 45 per cent of total investment.

As a percentage of output, the value of production of the service industries accounts for only 57 per cent of territorial GDP, versus 61 per cent of national GDP for the Canadian service sector as a whole. At the same time, service industries account for 82 per cent of total employment, much higher than the Canadian average. This condition arises because of the capital-intensive nature of goods production in the Northwest Territories, especially mining and oil and gas. Goods producing industries pay higher wages, require higher profits and generate greater depreciation than service industries. In consequence, the value-added per employee is much higher in the goods producing industries than the service industries.

These service industries - tourism, finance, insurance, personal and business services, trade, communications, transportation and government - have been the source

CHART B2
GROSS DOMESTIC PRODUCT BY INDUSTRY, NWT
1988



Source: GNWT Bureau of Statistics

of new job growth over the past several years. While employment in the goods producing industries has fallen since 1984, service sector employment has increased by 25 per cent. This is equivalent to a gain in net employment of approximately 660 jobs a year.

Similarly, as the value of output of the goods producing industries has declined by 16 per cent between its peak in 1985 and 1988, output in the service sector rose over the same period by 24 per cent.

In large measure, the continued growth in the service sector reflects the lack of sensitivity of service sector industries to cyclical economic behaviour. This feature of the service economy provides for greater overall economic stability during downturns and upswings in the economy.

Government dominates the service sector. In 1988, government employment, broadly defined, accounted for 54 per cent of total service sector employment, providing wages of $321 million. Government and related institutions are projected to account for over $320 million in investment in 1989, an increase of 17 per cent over 1988 and about one third of all investment in the Northwest Territories.

The trade industries in the Northwest Territories, including retail and wholesale trade, are major employers. Employment in the trade industries is forecast to have grown

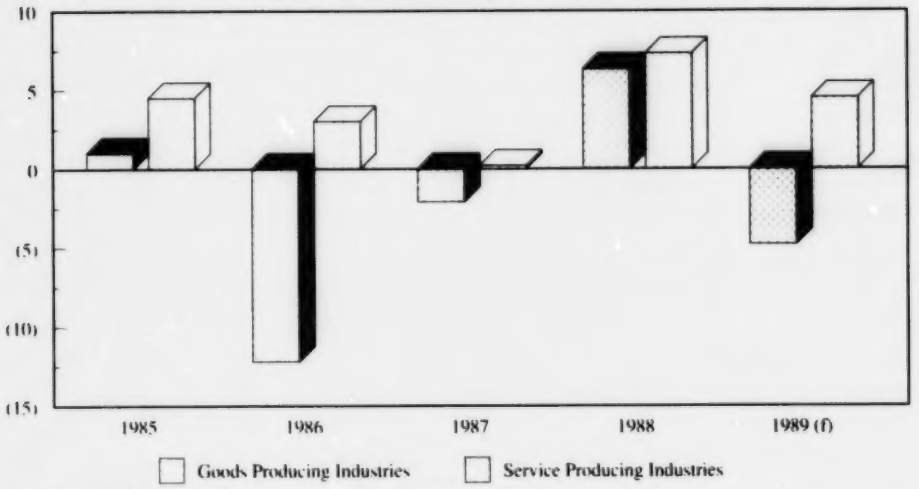
5.7 per cent in 1989 to 2,430, double the rate of employment growth for the Northwest Territories as a whole.

The retail trade industries benefited from relatively strong retail sales in 1989. Retail sales are forecast to have increased by 14 per cent in nominal terms, well above the projected 5.1 per cent increase in retail sales for Canada as a whole.

CHART B3

EMPLOYMENT, NWT, 1985-1989

(per cent change from previous year)



(f) Department of Finance Forecast

Source: Statistics Canada

TOURISM

The tourism and hospitality industries are amongst the fastest growing in the Northwest Territories. It is estimated that, in 1986, almost 2,800 person-years of employment were generated by these industries. The total number of hospitality businesses in the Northwest Territories has doubled between 1979 and 1988, reflecting the increased interest in the north as a travel destination for tourists and increased business travel.

The weaker economic conditions forecast for North America in 1990 may be reflected in poorer tourism expenditures in the north this year. Generally, vacation and pleasure travel spending are correlated with overall economic conditions.

TABLE B1
NORTHWEST TERRITORIES ECONOMIC INDICATORS

	1986	1987	1988	1989
Population (thousands) [a]	52.0	52.0	52.3	53.3
Income & Expenditure - $ (millions) [b]				
- Gross Domestic Product	1,745	1,794	1,824	n.a.
- Goods Producing Sector	880	825	789	n.a.
- Service Producing Sector	875	983	1,052	n.a.
- Final Domestic Demand	2,139	1,914	2,160	n.a.
Employment & Earnings				
- Employment (thousands)	18.7	18.6	19.9	20.4[g]
- Goods Sector (thousands)	3.7	3.7	3.9	3.7[g]
- Service Sector (thousands)	15.0	14.9	16.0	16.7[g]
- Unemployment Rate % [c]	14	n.a.	n.a.	16
- Average Weekly Earnings $	593	610	621	668[g]
- Total Personal Income - $ (millions)	1,030	1,057	1,144	n.a.
Investment & Production - $ (millions)				
- Total Investment [d]	1,070	789	881	963
- Retail Sales	251	256	285	325[g]
- Mineral Shipments	788	869	936	n.a.
- Fuels	120	156	170	n.a.
- Other Minerals	668	713	766	n.a.
- Fish Production [e]	1.65	2.06	2.67	2.09[g]
- Fur Production [f]	3.23	5.62	6.12	4.44
Consumer Price Index (% Change)	5.0	3.0	2.9	3.9

(a) Population as of July 1 in each year
(b) GDP and FDD at market prices, service and goods producing at factor cost
(c) 1986 is June census, 1989 is Bureau of Statistics January-March Survey
(d) Statistics Canada, Public and Private Investment in Canada
(e) Figures for May 1 - April 30 season
(f) Figures for July 1 - June 30 season
(g) Department of Finance forecast
n.a. = not available

APPENDIX C

GOVERNMENT EXPENDITURES

EXPENDITURE GROWTH AND FORMULA FINANCING

The five years from 1985-86 to 1989-90 cover the period of the original Formula Financing Arrangement between the Government of the Northwest Territories and Canada. One of the major principles underlying the Arrangement was that the territorial government would have the ability to establish its own budgetary priorities.

The proxy chosen to reflect the growth of territorial expenditure requirements under the original formula was the growth rate of provincial and local government spending. In the absence of deficit financing or surplus accumulation, the growth rate of total government expenditure should be roughly equal to the growth in provincial and local government expenditures. However, because the Government of the Northwest Territories assumed additional provincial-type responsibilities during the last five years, it is misleading to directly compare the growth of territorial and provincial spending since 1985-86.

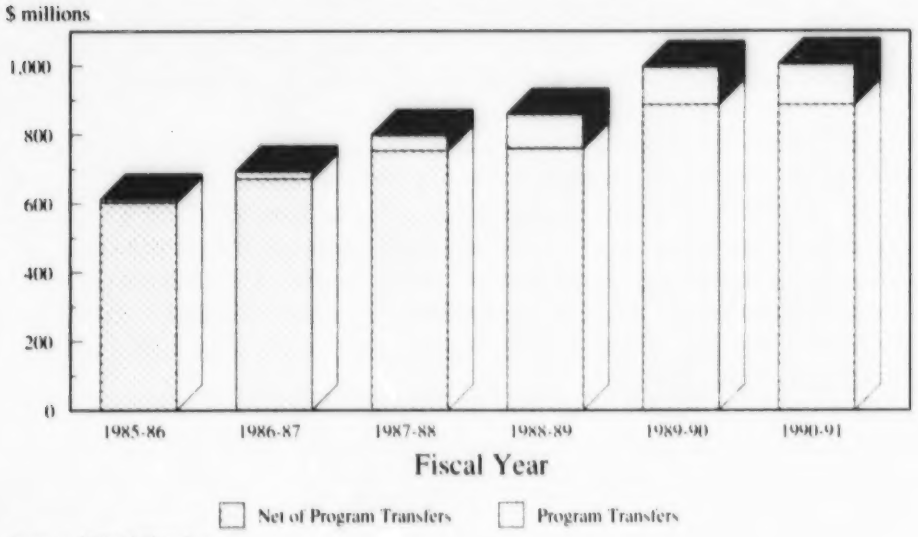
The transfer of a program involves the devolution of responsibility for program delivery, including responsibility for the allocation of resources to that program. Examples of major program transfers include health services in 1988-89 ($49.4 million) and forestry management and fire suppression in 1987-88 ($24.1 million). These transfers are part of a general process of devolution of powers from the federal to the territorial level of government, and as such contribute to the development of accountable government in the Northwest Territories.

When a program is transferred, a negotiated amount is added to the Government of the Northwest Territories' expenditure base, as defined in the Formula. Therefore, the increased expenditure responsibility is accompanied by a corresponding increase in revenues, at least in the initial year. In subsequent years, this amount is increased at the rate of increase in provincial and local government spending. However, actual government expenditures on the transferred program may differ from this. To compare Government of the Northwest Territories expenditure growth with that of other jurisdictions, program transfers must therefore be excluded.

Net of program transfers, the average growth rate of territorial government spending from 1985-86 to 1990-91 is 7.9 per cent. On a per capita basis, it is approximately 7 per cent. These figures are comparable with the growth rates of provincial and territorial expenditures as a whole, which should average 6.5 per cent annually, or 5.4 per cent on a per capita basis, over the same period.

If program transfers are included in territorial expenditures, the average growth rates are 10.4 and 9.4 per cent respectively. Chart C1 shows program transfers as a proportion of annual government expenditures over the last six years.

CHART C1
GOVERNMENT EXPENDITURES



Source: 1990-91 Main Estimates
Public Accounts

GOVERNMENT EXPENDITURES ON ECONOMIC DEVELOPMENT

The Government of the Northwest Territories has long recognized that the territorial economy, although strong and growing in some sectors, has serious weaknesses and imbalances which must be addressed. For this reason, the Government has allocated, and continues to allocate, a large portion of its resources toward economic development.

Most direct spending on economic development initiatives is channelled through the Department of Economic Development and Tourism, which in 1990-91 will spend an estimated $38.8 million. This represents an increase of 5.5 per cent over 1989-90 levels, an increase significantly larger than that in total government spending. The Department has been allocated a $9.2 million capital budget in 1990-91, an increase of $5.8 million over the current year. Much of this will be used to provide tourist facilities. The Northwest Territories Development Corporation, scheduled to be established at the beginning of the fiscal year, will allow the Government to actively participate in business development, either as the sole investor, or by providing equity capital in joint ventures with the private sector. The Corporation has been allocated an initial $2 million in investment capital in 1990-91.

Government spending on the development of the economy, however, is not limited to one department.

The Government of the Northwest Territories will allocate almost $182 million to the Department of Education in 1990-91, an increase of 6.2 per cent from 1989-90. One of the major roadblocks to increasing the employment of northerners in the Northwest Territories has been the lack of appropriate education, training and skills. A large portion of the population has not attained minimum levels of education. Almost $2 million in new funding has been allocated to programs designed to provide training and jobs to northerners. Funding for the Student Financial Assistance Program will increase by more than $600,000 to provide scholarships and enhanced benefits in recognition of the higher living costs faced by post-secondary students.

The funds allocated to education, whether for adult upgrading or for elementary schools, go toward the creation of an educated and skilled labour force. The largest potential for reducing unemployment is by educating and training Northwest Territories residents to fill existing and future jobs.

Transportation is another vital element in the development of the Northwest Territories economy. Long distances and limited access greatly increase the costs of doing business in the Northwest Territories and retard economic development. Significant improvements in communication and transportation have been made in recent years to reduce these constraints to economic development, and more is being done. The Government has allocated $37 million to the Department of Transportation in 1990-91.

The Department of Renewable Resources will spend an estimated $43.6 million in 1990-91. The Department encourages the sustainable development of wildlife and forest resources in support of the renewable resource sector of the economy.

The Department of Energy, Mines and Petroleum Resources has taken the lead role toward completing the Northern Accord, a major step to secure the control of the Northwest Territories' oil and gas resources. The Department will be allocated $3.8 million in 1990-91.

These five departments will have a combined budget of $304.8 million, or 30.4 per cent of total government expenditures, in 1990-91.

This does not represent the full amount of government spending targeted at economic development. Other government departments, through their purchasing, construction, maintenance and leasing policies have improved business development and employment opportunities for northerners. For example:

- In 1988-89 the Department of Public Works issued construction, maintenance

and service contracts valued at about $46 million, of which 88 per cent went to northern contractors. In addition, 95 per cent of contracts valued at $7 million for architecture and engineering services contracts were awarded to northern contractors.

- Fifty per cent of goods contracts valued at approximately $27 million were issued by the Department of Government Services to northern suppliers.

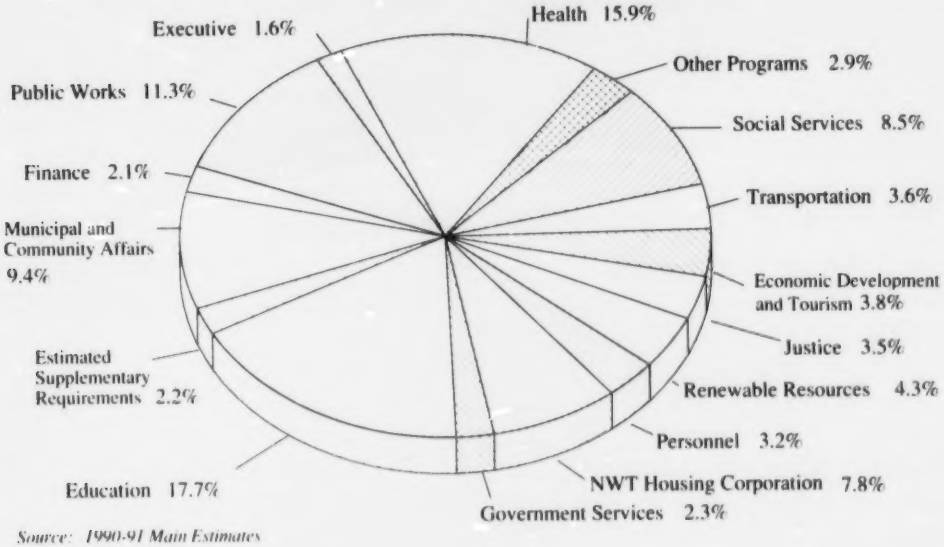
- Ninety per cent of the Northwest Territories Housing Corporation's 1988-89 expenditures for supplies and services for all capital projects, totalling approximately $21 million, went to northern contractors and suppliers.

In 1990-91 these three departments will be allocated a total of $218.3 million, or 21.8 per cent of the Government's total budget.

FISCAL SUMMARY

Total 1990-91 voted expenditures of the Government of the Northwest Territories are projected to be $1,001.2 million, an increase of $5.4 million over 1989-90 levels. After estimated supplementary appropriations and lapses are accounted for, expenditures will increase by $26 million, or 2.7 per cent increase, over 1989-90 expenditure levels. Given expected inflation of 4 to 5 per cent, this $26 million represents a real decline in expenditures. Capital spending will total $161.3 million, or 16.1 per cent of total expenditures and $839.9 million, or 83.9 per cent, will be allocated to operations and maintenance (O&M). Table C1 provides a summary of overall expenditure and revenue levels. Table C2 summarizes expenditures by department.

CHART C2
GOVERNMENT EXPENDITURES BY PROGRAM, 1990-91



Source: 1990-91 Main Estimates

TABLE C1
GOVERNMENT OF THE NORTHWEST TERRITORIES
THREE-YEAR SUMMARY OF REVENUES AND EXPENDITURES
$ (millions)

	1990-91 Main Estimates	1989-90 Revised Forecast	1989-90 Main Estimates	1988-89 Actuals
Revenues	984.2	955.5	943.0	876.8
Expenditures	1,001.2	995.8	934.7	858.0
Estimated Lapses less Supplementary Requirements	(0.4)	20.3	(19.7)	-
Surplus (Deficit)	(17.5)	(20.0)	(11.4)	18.7
Accumulated Surplus Opening Balance	41.9	66.9	61.2	41.8
Allocated to Loan Funds	-	(5.0)	(2.5)	(0.5)
Prior Year Adjustments	-	-	-	6.8
Surplus (Deficit) for the year	(17.5)	(20.0)	(11.4)	18.7
Projected Accumulated Surplus	24.4	41.9	47.2	66.9

Source: 1990-91 Main Estimates
Public Accounts

TABLE C2
THREE-YEAR EXPENDITURE SUMMARY BY PROGRAM
$ (thousands)

PROGRAM	1990-91 Main Estimates	1989-90 Revised Forecast	1989-90 Main Estimates	1988-89 Actuals
Legislative Assembly	8,686	8,783	6,245	5,966
Executive	16,852	18,536	15,862	14,901
NWT Housing Corporation	79,919	82,555	79,744	70,880
Finance		21,275	21,569	20,765
18,701				
Culture & Communications	11,733	12,201	11,676	7,532
Personnel	32,406	31,133	28,038	27,081
Justice	35,812	35,343	31,746	32,962
Safety & Public Services	5,465	5,222	4,917	3,926
Government Services	23,150	24,785	24,226	21,833
Public Works	115,245	109,329	107,406	105,121
Transportation	37,028	37,352	35,103	32,529
Renewable Resources	43,632	51,903	40,739	38,631
Municipal & Community Affairs	95,995	103,977	99,325	77,410
Health		162,387	158,698	154,496
149,323				
Social Services	87,446	84,816	77,500	73,202
Energy, Mines & Petroleum Resources	3,792	3,864	3,164	2,678
Economic Development & Tourism	38,768	36,758	35,813	28,826
Education	181,617	170,948	157,939	146,539
Total O & M and Capital	1,001,208	995,772	934,704	858,041
Projects on behalf of Third Parties	46,530	46,930	35,828	35,990
Total Expenditures	1,047,738	1,042,702	970,532	894,031

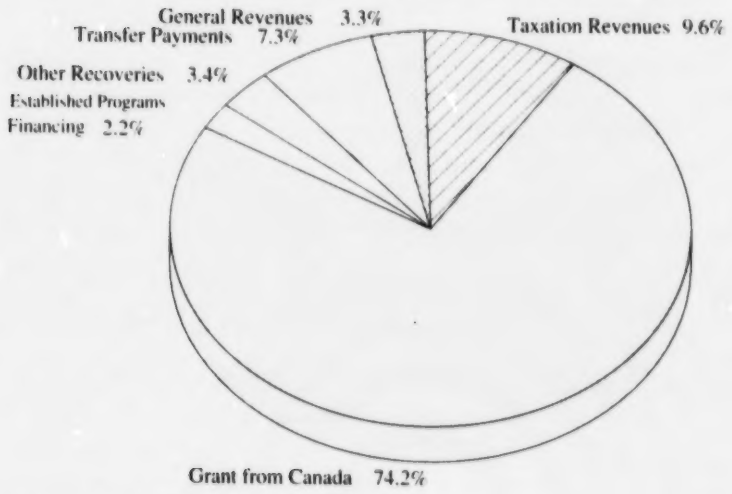
Sources: Public Accounts
1990-91 Main Estimates

APPENDIX D

GOVERNMENT REVENUES

Total revenues of the Government of the Northwest Territories, excluding revenues from projects undertaken on behalf of third parties, are expected to grow by 3.0 per cent in 1990-91 to $984 million. This growth is much lower than experienced over the previous four years because of the reduction to the growth in the grant from Canada. Table D1 summarizes the revenues of the Government of the Northwest Territories from 1985-86 to 1990-91. Chart D1 shows the distribution of 1990-91 revenues.

CHART D1
GOVERNMENT REVENUES, 1990-91
percentage distribution



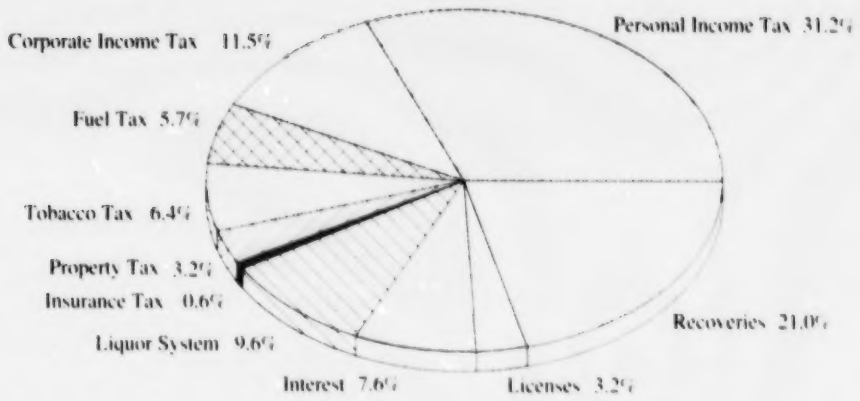
Source: 1990-91 Main Estimates

The grant from Canada is expected to be $22 million higher in 1990-91 than in 1989-90, a 3.1 per cent increase. Under the previous formula, the grant would have grown by $47.6 million, or 6.7 per cent.

The government's 1990-91 own-source revenues (all revenues except transfer payments from the federal government and work performed on behalf of third parties) are expected to total $160.4 million. This represents growth of 7.9 per cent over their 1989-90 levels. This growth is due to increases in both tax revenues and general revenues. Chart D2 shows the distribution of projected own-source revenues of the government for the 1990-91 year.

CHART D2
OWN-SOURCE REVENUES, 1990-91

percentage distribution



Source: 1990-91 Main Estimates

Revenues from the Northwest Territories Liquor Commission will increase by 17 per cent, due primarily to the mark-up increases announced in this budget.

Taxation revenues are estimated to reach $94 million in 1990-91, an increase of 14.2 per cent over the current year. While all tax revenues are expected to increase, most of the overall increase is due to higher corporate incomes, personal incomes and tobacco prices. Of the 14.2 per cent increase in tax revenues, 4.2 percentage points are due to the tax increases announced in this budget. The remaining 10 percentage points are due to volume or price increases.

Tobacco tax revenues increased significantly in 1989-90 due to an increase in the Northwest Territories tax rate from 45 to 55 per cent of the Yellowknife price effective April 1, 1989. 1990-91 tobacco tax revenues are expected to be 42 per cent higher than their 1989-90 Main Estimate level. Eleven percentage points of this increase are due to the tax increases announced in this year's budget. The remainder is due to price changes. Since the tax is calculated as a percentage of the price, the increase in the federal tax announced in the April, 1989, federal budget causes Northwest Territories tax collections to increase.

Corporate and personal income tax revenues of the Government of the Northwest Territories are very volatile from year to year. A large portion of the corporate income tax revenues of the Northwest Territories continues to come from a limited

number of taxpayers in the oil and gas and mining sectors. Our tax collections will continue to fluctuate with the fortunes of these industries.

Income taxes are collected by Revenue Canada under a tax collection agreement between the governments of Canada and the Northwest Territories. The amounts due in any given year are re-estimated throughout the year, and adjustments to payments are made in following years. This payment method amplifies year-to-year fluctuations in tax receipts and this is especially evident in the Northwest Territories where tax collections are very volatile.

Corporate income tax revenues for the 1985-86 and 1986-87 years were significantly higher than in previous years, due primarily to over-estimates for those years by Finance Canada and substantial positive adjustments for prior years. Income tax revenues for the 1987-88 and 1988-89 years therefore reflected over-payments of taxes from prior years and were artificially low.

Personal income tax revenues have also increased substantially since 1987-88. Higher personal income tax revenues are due in part to the taxation of northern allowances starting in 1987. On average, Northwest Territories taxpayers have been paying higher federal income taxes since 1987 because housing allowances and subsidized employer housing are now taxed. Although taxpayers receive a tax deduction of up to $5,400 annually for housing, in many cases this deduction does not offset the increased taxation of housing benefits. This has increased both federal and Northwest Territories income taxes since Northwest Territories income tax is set as a percentage of the federal tax. However, the housing deduction is now available to all taxpayers, thereby making the system more equitable than under the previous remission orders.

TABLE D1
SIX-YEAR REVENUE SUMMARY BY SOURCE

$ (000)

	1985-86 Actuals	1986-87 Actuals	1987-88 Actuals	1988-89 Actuals	1989-90 Revised Forecast	1990-91 Main Estimates
Grant from Canada	440,455	498,989	572,213	657,499	707,684	729,684
Taxation Revenue						
Individual Income Tax	43,955	38,528	39,550	45,311	47,325	50,424
Corporate Income Tax	18,150	19,760	5,542	(123)	13,405	18,782
Fuel Taxes	11,002	9,670	8,982	9,186	9,101	9,323
Tobacco Taxes	4,426	4,698	5,362	5,337	7,055	9,994
Property Taxes	2,945	3,746	4,927	4,508	4,785	4,780
Insurance Taxes	548	643	636	689	640	720
	81,026	77,045	64,999	64,908	82,311	94,023
General Revenues						
Liquor Control System	10,075	10,180	10,484	11,531	13,097	15,322
Interest Income	9,291	10,882	9,475	12,369	9,508	11,891
Licenses, Fees and Permits	4,146	3,942	4,411	4,666	5,084	5,463
	23,512	25,004	24,370	28,566	27,689	32,676
Established Programs Financing	14,573	17,062	24,705	21,186	23,182	21,765
Other Transfer Payments	48,114	48,325	53,891	68,821	75,916	72,327
Recoveries	26,251	36,500	29,019	35,781	38,694	33,706
Total Revenues	633,931	702,925	769,197	876,761	955,476	984,181
Projects on Behalf of Third Parties	26,961	30,827	46,886	35,990	46,930	46,530
Total	660,892	733,752	816,083	912,751	1,002,406	1,030,711

Source: 1990-91 Main Estimates
Public Accounts

REVENUE INITIATIVES

PERSONAL INCOME TAX

Effective January 1, 1990, the Northwest Territories personal income tax rate will be increased by one percentage point to 44 per cent of Basic Federal Tax. Source deductions for this increase will begin on July 1, 1990. Because source deductions

at the higher rate will cover only half the year, tax will be deducted at the rate of 45 per cent from July 1, 1990, to December 31, 1990. Effective January 1, 1991, the rate for source deductions will be reduced to 44 per cent. The increase in the personal income tax rate will increase revenues by $1.3 million in 1990-91.

Table D2 illustrates the additional tax payable as a result of this measure for taxpayers at various income levels in the Northwest Territories.

TABLE D2
ADDITIONAL INCOME TAX PAYABLE BY NWT TAXPAYERS
PERSONAL INCOME TAX INCREASE TO
44% OF BASIC FEDERAL TAX

INCOME	TAXPAYER WITH NO DEPENDANT	MARRIED TAXPAYER SUPPORTING SPOUSE AND TWO CHILDREN
$15,000	$ 9	$ 0
$30,000	$ 34	$ 20
$45,000	$ 72	$ 57
$60,000	$111	$ 94
$75,000	$155	$137

CORPORATE INCOME TAX

Effective January 1, 1990, the Northwest Territories corporate income tax rate will be increased from 10 per cent of taxable income to 12 per cent of taxable income. At the same time, a new lower rate of 8 per cent will be introduced for the first $200,000 earned by Canadian-controlled private corporations. The net effect of these tax changes will be an increase of $1.4 million in corporate income tax revenues of the Government of the Northwest Territories.

With these changes, all private Canadian-controlled corporations with income under $400,000 operating in the Northwest Territories will pay less tax. A company with a taxable income of $200,000 will save $4,000.

TOBACCO TAXES

This budget increases the tax paid on cigarettes, cigars, and other tobacco products from 55 per cent to 60 per cent of the Yellowknife price, effective April 1, 1990. This change will increase the price of a carton of cigarettes by about $1.00, with corresponding increases in the price of other tobacco products.

The tax rate on loose cigarette tobacco will also be increased, but the increase will be phased in. Cigarette tobacco is now taxed at 25 per cent of the price. This rate

was scheduled to increase to 40 per cent on April 1, 1990, and to 55 per cent on April 1, 1991. The rate will still be increased to 40 per cent on April 1 of this year.

Tobacco tax revenues will increase by an estimated $759,000 in 1990-91 as a result of these increases.

LIQUOR PRICING

The mark-ups on alcoholic beverages sold by the Northwest Territories Liquor Commission will be revised effective April 1, 1990. The mark-up on beer will be increased from 100 per cent to 110 per cent. The mark-up on all other items will increase from 150 per cent to 170 per cent. Since, with the exception of liquor licence fees, all government revenue from liquor comes from the profits of the Liquor Commission, the mark-up increases are equivalent to tax increases on these products. These changes will increase the price of beer by five per cent and of spirits and wines by eight per cent. Government revenues will increase by $1.85 million as a result of these increases.

Table D3 summarizes the revenue impact of the various tax changes and alcohol mark-up increases.

TABLE D3
IMPACT OF BUDGETARY REVENUE MEASURES, 1990-91

	REVENUE CHANGE 1990-91
Corporate Income Tax	
Rate reduction on first $200,000 of income for private, Canadian-controlled corporations to 8 per cent from 10 per cent	$ (800,000)
General Rate increase for all other corporate income from 10 to 12 per cent of taxable income	$2,200,000
SUBTOTAL	$1,400,000
Personal Income Tax	
Rate increase from 43 to 44 per cent	$1,300,000
Tobacco Tax	
Rate increase from 55 to 60 per cent of price, for cigarettes, cigars and other tobacco.	$ 759,000
Alcohol Mark-ups	
Spirits: Increase from 150 to 170 per cent	$1,000,000
Wine: Increase from 150 to 170 per cent	$ 200,000
Beer: Increase from 100 to 110 per cent	$ 650,000
SUBTOTAL	$1,850,000
TOTAL	**$5,309,000**

TABLE D4
MAJOR PROVINCIAL AND TERRITORIAL TAX RATES
AS OF JANUARY 1, 1990 (a)

Province/Territory	Personal Income Tax (%)	Retail Sales Tax (%)	Fuel Taxes: Gasoline Leaded (c/litre)	Fuel Taxes: Gasoline Unleaded (c/litre)	Fuel Taxes: Diesel	Fuel Taxes: Aviation	Tobacco Taxes: Cigarettes ($/ctn)	Tobacco Taxes: Tobacco (c/gram)	Annual Health Care ($)(m)	Payroll Tax (%)	Corporate Income Taxes (%): Small	Corporate Income Taxes (%): Large	Capital Tax (n) (%)
Northwest Territories	44.0	-	8.5 (h)	8.5	7.2	1.0	13.40 (k)	4.40 (k)	-	-	8	12	-
Yukon	45.0	-	4.2	4.2	5.2	0.7	6.40	1.14	-	-	5	10	-
British Columbia	51.5	6	11.0	9.0	9.5	2.8	11.52	4.40	216/456	-	9	14	-/2.0
Alberta	46.5 (b)	-	5.0	5.0	5.0	5.0	9.60	2.00	216/432	-	5	15	-
Saskatchewan	50.0 (c)	7	12.0	10.0	10.0	10.0	13.36	2.70	-	-	10	15	0.5/3.0
Manitoba	52.0 (d)	7	10.8	9.0	9.9	5.8	13.00 (j)	4.30	-	2.25	10	17	0.3/3.0
Ontario	53.0 (e)	8	14.3	11.3	10.9	2.1	7.66 (j)	2.20	-	1.95	10	15.5	0.3/0.8
Quebec	N/A (f)	9	14.4 (i)	14.4	12.5	9%	9.04	2.00	-	3.36	3.36	6.16	0.5/1.0
New Brunswick	60.0	11	12.1	10.3	11.1	2.2	13.60 (j)	3.96	-	-	9	16	-/3.0
Nova Scotia	56.5	10	9.0	9.0	8.8	0.8	9.00 (j)	3.50	-	-	10	15	-/1.5
Prince Edward Island	57.0 (g)	10	9.2	9.2	9.4	0.7	9.40	1.70	-	-	10	15	-/1.5
Newfoundland	62.0	12	12.2	10.7	12.3	0.7	10.40 (j)	3.50	-	-	10	17	-/2.0
Canadian Average (l)	52.4	7.4	12.5	11.0	10.5	3.1	9.37	2.6		1.66	7.7	13.0	0.3/1.2
Average including Sales Tax							10.59 (j)	3.0					

- No tax levied.

(a) Northwest Territories tax rates reflect rate changes included in the budget.

(b) In addition, Alberta imposes a flat tax of 0.5% of income and a surtax of 8% of provincial tax over $3,500.

(c) In addition, Saskatchewan imposes a flat tax of 2% of income and a surtax of 12% of provincial tax over $4,000.

(d) In addition, Manitoba imposes a flat tax of 2% of income and a surtax of 2% of income over $30,000.

(e) In addition, Ontario imposes a surtax of 10% of provincial tax over $10,000.

(f) Quebec levies a personal income tax directly against net income.

(g) Prince Edward Island imposes a surtax of 10% of provincial tax in excess of $12,500.

(h) A lower rate of 5.1 cents applies to communities not served by the highway system.

(i) A lower rate of 9.6 cents applies to areas near the border and a lower rate of 12.0 cents applies to northern Quebec.

(j) In addition, Manitoba, Ontario, New Brunswick, Nova Scotia and Newfoundland apply provincial sales tax to sales of tobacco. The Canadian average tax rate is $10.59 per carton of cigarettes when provincial sales tax is included.

(k) Northwest Territories cigarette and tobacco taxes are estimated taxes as of April 1, 1990. A lower rate of 2.9 cents per gram will apply to tobacco used to roll cigarettes in the NWT.

(l) Average of all provincial and territorial rates, weighted by population.

(m) Rates shown for health care premiums are for single individuals and families of three or more.

(n) Rates shown for the capital tax are for large corporations and for financial institutions in the order shown. The bases are different for the different types of companies.

APPENDIX E

THE
FORMULA FINANCING
ARRRANGEMENT

The purpose of this Appendix is to explain the workings of the Formula Financing Arrangement through which the yearly grant from Canada was determined during the years 1985-86 to 1989-90 and to outline the new Formula that was introduced by the federal government for the period starting in 1990-91.

BACKGROUND

A Formula Financing Arrangement between the Governments of Canada and of the Northwest Territories was first implemented for the 1985-86 fiscal year. Prior to the Formula, a yearly "deficit grant" was determined through bilateral negotiations between the federal and territorial governments as part of the federal budgetary process. This grant was established as the difference between an agreed upon level of territorial expenditures and expected territorial revenues.

As part of the evolution of northern governments accountable to the residents of the north, a funding method was developed which would provide cash transfers from the federal government to the governments of the two territories, similar to the way the federal Equalization program provides transfers to some of the provinces, albeit calculated in a considerably different manner.

Grants to the Northwest Territories could not be governed by Equalization. The Equalization formula assumes that the per capita costs of providing public goods and services is comparable from one province to another. Equalization is therefore built on the premise that as long as equalization payments compensate receiving provinces for the difference between their revenue raising capacity and a national standard revenue raising capacity, these provincial governments will "...have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation." (Constitution Act, 36(2)).

Under the Equalization formula, the Government of the Northwest Territories would not be entitled to receive Equalization payments since its fiscal capacity, as calculated under the Equalization program, would exceed the national standard. Yet the gap between fiscal capacity and expenditure needs is wider in the the Northwest Territories than in any of the provinces. For the current fiscal year, the Government of the Northwest Territories' own-source revenues amounted to approximately $2,800 per capita while the Government's per capita expenditures were $18,700. This reflects the extremely high costs in Canada's north. These high costs are partially explained by the need to provide government services to more than sixty communities, most of which have less than five hundred residents. These communities are

scattered over 3.3 million square kilometres. The high costs are also explained by high transportation costs, especially in areas with no year-round road access, and by high utility costs. There is also a relatively high demand for capital infrastructure in view of the Northwest Territories early stage of economic development and high population growth rate.

Including the territories in the Equalization system would therefore require changing the Equalization formula. The current formula uses revenue raising capacity as a proxy for a jurisdiction's capacity to provide "reasonably comparable levels of public services at reasonably comparable levels of taxation". It would have to be changed to a formula that would directly incorporate measures of cost differences between the regions of Canada, or at least between the territories and the provinces.

THE FIRST FIVE YEARS - 1985-86 TO 1989-90

The formula that governed the grant to the Government of the Northwest Territories from 1 April, 1985, to 31 March, 1990, was an expenditure-based formula. In its simplest expression, the formula used a given expenditure level at a particular date, the "expenditure base", which was then escalated yearly to reflect increases in Canadian provincial and local government expenditures. From the expenditure base determined for a budget year was subtracted the own-source revenues that could be collected by the Government of the Northwest Territories if it maintained its tax rates at predetermined and fixed levels; other transfers from the federal government were also subtracted. The resulting figure yielded the yearly grant from Canada. A numerical example of the calculation is given in Table E1.

THE EXPENDITURE BASE

The expenditure base in the first year was equal to the level of expenditure of the Government of the Northwest Territories in the fiscal year 1982-83. For the purposes of calculation, 1982-83 revenues were used as a proxy for that year's expenditures. This expenditure base was then adjusted yearly by applying to it a percentage growth that was equal to the percentage growth in the total expenditures of all Canadian provincial and local governments. To smooth out potentially large and volatile year-over-year changes in the growth rates of total Canadian provincial and local government expenditures, a three-year average of the growth rate was used - in mathematical terms, this is referred to as a three-year arithmetic moving average. This yearly adjustment factor to the expenditure base, called the "escalator", was first applied to the 1982-83 expenditure base and each subsequent year up to 1985-86 to determine the size of the expenditure base in the first year of the Formula. It was then applied in the subsequent years 1986-87 to 1989-90.

The choice of the escalator relied on a straightforward principle. Since the responsibilities of the territorial governments were similar to those of provincial and local governments, the growth in these latter governments' expenditures could be used as a proxy for the growth in the territories' expenditure base.

TERRITORIAL OWN-SOURCE REVENUES

The second main component of the Formula, territorial own-source revenues, included virtually all those existing revenue sources over which the Government of the Northwest Territories had direct control. For any given year, these revenues were measured using fixed tax rates that were in force on 31 March, 1985, and multiplying these rates by the given year's volumes. The resulting revenues are referred to as "hypothetical own-source revenues" or "eligible revenues" and the use of 31 March, 1985, tax rates as the "fixed tax rate" principle.

This approach was intended to achieve two main objectives. Firstly, it stabilized territorial revenues by eliminating the effects of wide fluctuations in tax revenues which are inherent in economies with narrow and volatile tax bases such as the Northwest Territories. The formula achieved this since all increases or decreases in tax collections that were due to changes in economic conditions or in federal tax policies were accompanied by compensating decreases or increases in the grant, as is evident from Table E1.

Secondly, it clearly recognized that if the Government of the Northwest Territories wished to enhance its programs and needed to fund expenditures beyond what was provided under the Formula, it would have to increase its tax rates. The Formula ensured this result since the revenue effect of tax rate initiatives, either the introduction of new taxes or changes to existing tax rates, did not affect territorial hypothetical own-source revenues for purposes of calculating the grant. The effects of such changes were treated as outside the formula.

The 1985 Agreement was signed for an initial period of three years and included a clause that provided for a two-year extension by mutual consent of the parties. A review of the Formula was therefore undertaken by the two orders of governments in 1987. It resulted in the federal government introducing a change to the escalator: as of the 1988-89 fiscal year, the level of the escalator was not to exceed the three-year average rate of growth of nominal Canadian Gross Domestic Product. As a result of this change, if the growth rate in provincial and local government expenditures exceeded the rate of growth of the Canadian economy, i.e., if provincial and local governments increased their share in total economic activity, the grant to the territories would be insufficient to allow them to keep pace with the growth in provincial expenditures.

1990-91 AND BEYOND

On 21 December, 1989, the federal government announced that it was introducing some fundamental changes to the Formula. These changes result in a grant determination formula which radically alters the Government of the Northwest Territories' fiscal outlook and the basic principles underlying the previous Formula Financing Arrangement.

Three major changes were made to the Formula:

1. The expenditure base will be adjusted for the growth in the population of the Northwest Territories, compared to that of Canada as a whole;

2. Territorial own-source revenues used in calculating the grant will be adjusted, for the duration of the Arrangement, by a fixed factor reflecting territorial "tax effort" relative to the average provincial tax effort. Territorial tax effort will be measured by the Representative Tax System, as explained below, used for determining entitlements under federal-provincial Equalization;

3. Territorial own-source revenues used in calculating the grant will be further adjusted, on a yearly basis, by a variable factor reflecting year-over-year changes in provincial tax effort.

A numerical example of the calculation is given in Table E2.

THE EXPENDITURE BASE

The expenditure base will be equal to 1982-83 actual expenditures escalated by the three-year average growth in total provincial and local government expenditures, as in the previous formula. However, starting in 1990-91, the base will also be adjusted for the rate of growth of the population of the Northwest Territories relative to the rate of growth of the population of Canada. The relative rates of growth will also be averaged over three years to smooth out some of the volatility in territorial population changes and to put this adjustment factor on the same base as the provincial and local government expenditure escalator.

The result of this new adjustment factor is that for each percentage point difference between the rate of growth of the Northwest Territories and Canadian populations, the expenditure base will be adjusted by approximately one percentage point. Therefore, if population in the Northwest Territories and in Canada grow at, say, 2 and 1 per cent per year, respectively, the expenditure base will grow by roughly 1 percentage point more than the provincial and local expenditure escalator. This change is equivalent to expressing the growth in the expenditure base on a per capita basis.

TERRITORIAL OWN-SOURCE REVENUES

Territorial hypothetical own-source revenues, for purposes of calculating the grant, will be adjusted by two separate factors and the tax rates will be re-based from those of 31 March, 1985, to the tax rates of 31 March, 1988.

The first adjustment factor is based on the Northwest Territories' 1987-88 tax effort. It is a tax effort adjustment factor. The tax effort adjustment factor is equal to the ratio of the Northwest Territories fiscal capacity relative to actual tax collections. Fiscal capacity is a measure of what Government of the Northwest Territories own-source revenues would be if, on average, the government taxed the same things as the provinces and taxed them at the same rate.

The Northwest Territories' fiscal capacity was estimated by the same method as is used under the Equalization program. This is done by calculating the Northwest Territories' tax bases using the standardized definitions developed for Equalization. The bases are then multiplied by National Average Tax Rates, as also calculated under the Equalization program, to yield fiscal capacity. Dividing fiscal capacity by actual tax collections yields a 1987-88 tax effort adjustment factor of approximately 1.40. This factor is to remain fixed for the duration of the Arrangement. It is referred to as a revenue "catch-up" factor.

The second adjustment factor is a measure of year-over-year changes in provincial and local government tax effort. Starting in 1990-91, own-source revenues will be further adjusted, for purposes of calculating the grant, by a factor equal to the percentage change in the tax effort of provincial and local governments since 1987-88. This factor is greater than unity, the estimates of its value ranging from 1.05 to 1.1 for 1990-91. It is referred to as a revenue "keep-up" factor.

The application of these two factors to hypothetical own-source revenues artificially increases the amount that is subtracted from the expenditure base in the calculation of the grant. Since the federal government realized that strict application of the adjustment factors would create fiscal chaos for the territories, it decided to arbitrarily reduce the value of the territorial tax effort factor by 15 per cent. Also, as a result of representations by the territorial governments, it decided to phase-in the tax effort factor's application over a three-year period. This 15 per cent reduction to the "catch up" reduces it to approximately 1.20 and the phase-in further reduces it to approximately 1.10 in 1990-91 and 1.15 in 1991-92.

SOME EFFECTS OF THE CHANGES

The most obvious effect of the change to the formula is the reduction in the grant. The large reduction in funding resulting from the artificial upward adjustment to Government of the Northwest Territories hypothetical own-source revenues for

purposes of establishing the grant cannot, in the medium term, be compensated for by a higher expenditure base due to higher Northwest Territories population growth.

Some of the other effects are less obvious but potentially more serious for the longer-term fiscal position of the Government of the Northwest Territories. Only one of these effects will be outlined here.

The new formula produces perverse effects with respect to changes in tax collections. Since hypothetical own-source revenues are adjusted upward, any increase in tax collections due to increases in the level of economic activity results in the grant decreasing by a larger amount. For example, if the combined effect of the two adjustment factors is to artificially increase hypothetical own-source revenues by a factor 1.30, a $1 increase in tax collections will cause the grant to fall by $1.30. This creates a fiscal disincentive to economic development and growth. Conversely, there is a net fiscal dividend to economic decline since a decline in hypothetical own-source revenues would be compensated by a larger increase in the grant. Under the previous Formula, changes in tax collections resulted in equal changes in the grant rather than being amplified as in the new Formula.

CONCLUSION

Formula Financing was a very important step in the constitutional development of the Northwest Territories. By providing a yearly unconditional grant to the Government of the Northwest Territories, it placed the responsibility for allocating budgetary resources with the elected territorial government.

The Formula agreed to by both governments and introduced in 1985 was innovative and worked well over the first five years. The changes introduced by the federal government for 1990-91 and beyond make the Formula much more complex. Projecting the grant for a given year previously required a projection of own-source revenues and of the provincial-local government expenditure escalator. It now also requires projections of changes in provincial and local government tax efforts. Projections of own-source revenues, which previously did not have any effect on the Government of the Northwest Territories' fiscal framework will now have the direct and perverse effect described above. The feature of the previous formula that recognized the need to insulate the Government of the Northwest Territories from the volatility of tax collections imputable to the volatile economic base is also gone, thereby increasing uncertainty over available funding. Overall, the new formula is a set-back in the financial arrangements between Canada and the Government of the Northwest Territories.

However, it maintains one of the key features of the previous financial arrangements by providing financing to the territories through a formula whose terms are fixed. It is therefore expected that the territories will not be vulnerable to further direct cuts in federal transfer payments over that period.

TABLE E1
CALCULATION OF THE GRANT UNDER
THE 1985-86 TO 1989-90 FORMULA

Expenditure base in year *t*	$500
TIMES	
Escalator (three-year average provincial-local government expenditure growth)	1.05
EQUALS:	
Expenditure base in year *t+1*	525
LESS:	
Hypothetical own-source revenues, (Revenues measured at March 31, 1985, tax rates)	$100
EQUALS: Grant from Canada	$425

Note: Changes in revenues due to changes in tax rates are outside of the formula and are therefore entirely to the benefit of the Government of the Northwest Territories.

TABLE E2
CALCULATION OF THE GRANT
UNDER THE NEW FORMULA

Expenditure base in year *t*			$500
TIMES			
Escalator (three-year average provincial-local government expenditure growth)			1.05
			$525
TIMES			
NWT population growth rate (= 1.02) / Canadian population growth rate (= 1.01)			1.01
EQUALS:			
Expenditure base in year *t+1*			$530.25
LESS:			
Hypothetical own-source revenues (Revenues measured at March 31, 1988 tax rates)			100
times			
NWT fiscal capacity in base year (1987-88) / GNWT tax collections in base year (1987-88)	times 0.85		1.20
times			
Total Canadian provincial and local government tax effort in current year / Total Canadian provincial and local tax effort in base year (1987-88)		=	1.08
			129.60
EQUALS: Grant from Canada			$400.65